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March 26, 1998

MEMORANDUM FOR DIRECTOR, USAID/Honduras, Elena Brineman

FROM: RIG/A/San Salvador, Wayne J. Watson

SUBJECT: Audit of USAID/Honduras' Review and Certification of Unliquidated Obligations for Project and Non-project Assistance, Report No. 1-522-98-004-F

This memorandum is our report on the subject audit. In finalizing the report, we considered your comments on the draft audit report and have included them in their entirety as Appendix II.

USAID/Honduras has taken final action on the three recommendations contained in this report. For Recommendation Nos. 1 and 3, Mission operating procedures were revised to strengthen its review of unliquidated obligations. Recommendation No. 2 cited $20,704 of excessive commitments, and the Mission has decommited those funds.

I appreciate the cooperation and courtesy extended to my staff during the audit.

Background

Concerned that Federal agencies were recording obligations in situations where no real obligation existed and that information on which to determine an agency's future funding requirements was not reliable, Congress, with the General Accounting Office and Office of Management and Budget, developed statutory criteria for determining the validity of an obligation. In order to-properly certify the validity and accuracy of obligated balances, agencies are required to verify their own accounts at least once each year. This verification is commonly referred to at USAID as the Section 13 11 review or certification, named after the section of the original authorizing public law.

This audit is part of the Office of the Inspector General's (OIG) worldwide review of USAID's obligations for project and non-project assistance. The OIG's Division of Performance Audits (IG/A/PA) is leading this worldwide effort, with the assistance of auditors from all OIG offices of Regional Inspectors General.

The worldwide audit is limited to obligations for project and non-project assistance which had unliquidated balances on September 30, 1996. It does not cover obligations funded with U.S.-owned local currency, obligations for disaster relief, or obligations maintained by USAID for the Trade and Development Agency.

IG/A/PA randomly selected USAID sites for detailed audit work and also determined the number of unliquidated obligations to be randomly selected and then reviewed at each site. A total of 19 sites (U&AID/Washington and 18 missions) were selected for review. USAID/Honduras was among those missions randomly selected for review.

Mission records indicate that, as of September 30, 1996, USAID/Honduras had 124 unliquidated obligations for project and non-project assistance with balances totalling $43,924,659. Of these, we randomly selected and reviewed 30 obligations, which had unliquidated balances totalling $14,5 10,589.

Audit Objective

As part of a worldwide audit, the Office of Regional Inspector General/San Salvador audited selected unliquidated obligations at USAID/Honduras as of September 30, 1996 to answer the following objective:

> Did USAID/Honduras review and certify its unliquidated obligations for project and non-project assistance in accordance with U.S. laws and regulations and USAID policies and procedures?

Appendix I describes in detail the audit's scope and methodology.

Audit Findings

Did USAID/Honduras review and certify its unliquidated obligations for project and non-project assistance in accordance with U.S. laws and regulations and USAID policies and procedures?

For the items tested, USAID/Honduras generally followed U.S. laws and regulations and USAID policies and procedures in reviewing and certifying its unliquidated obligations for project and non-project assistance; however, in order to fully comply with USAID procedures, the Mission needed to improve its review process by ensuring (i) a more effective application of USAID's forward funding guidance and (ii) proper documentation of its reviews.

The audit sample included 30 unliquidated obligations totalling $14,5 10,589 and 100 commitments' associated with these obligations. Review of these obligations and commitments showed that USAID/Honduras conducted monthly Section 13 11 reviews to ensure that unliquidated obligations and commitments were valid and still needed, making deobligations or decommitments when deemed appropriate. Unliquidated obligations were also properly certified as of September 30, 1996, and valid obligating documents were executed for all 30 obligations tested. However, as discussed below, thirteen unliquidated obligations and two unliquidated commitments had balances as of September 30, 1996, which exceeded USAID's forward funding guidance and, at the time of our field work, one commitment continued to have an excess balance of $20,704 which the Mission should take action to decommit. In addition, management controls needed improvement to ensure proper documentation of the reviews.

Some Obligations Had
Excessive Balances

Each year USAID's Bureau for Policy and Program Coordination issues guidance for the preparation of Mission and office budgets. Guidance applicable to the period under audit stated that budgets should be prepared as follows:

> New Activities Obligations should provide funding for at least the first 18 months, but not more than 24 months.
>
> Continuing Activities Obligations should be sufficient to fund anticipated expenses for no more than 12 months beyond the end of the fiscal year in which the obligation takes place.

We reviewed obligation balances as of September 30, **1996,** and applied USAID's guidance as follows:

> New Activities In general, obligation or commitment balances were considered reasonable if they did not exceed anticipated expenses for a period of 24 months following the date of obligation or commitment, or through September 30, 1997, whichever was later. Any questioned amount was discussed with appropriate Mission staff.

'GAO's *Principles of Federal Appropriations Law* defines an obligation as "some action that creates a liability or definite commitment on the part of the government to make a disbursement at some later time." USAID Financial Management Bulletin, Part II, No. 14A, defines a commitment as "funds set aside [for an obligation] to pay for the goods or services being procured."

Continuing Activities In general, obligation or commitment balances were considered reasonable if they did not exceed anticipated expenses for the 12-month period ending September 30, 1997, the expiration date of the obligating or commitment document, or the project assistance completion date, whichever was earlier. Balances were considered reasonable as of the time of our audit if they did not exceed the anticipated expenses through September 30, 1998. We also took into account balances of earlier or planned obligations which affected the continuing need for part or all of the unliquidated balance being audited. Any questioned amount was discussed with appropriate Mission staff.

In several instances, the Mission did not identify funds in the September 1996 Section 13 11 review which were excessive as of September 30, 1996. These funds were not identified, in part, because the Mission's operating procedures for Section 13 11 reviews did not include consideration of the Bureau for Policy and Program Coordination's budget guidance on forward funding to evaluate obligations and commitments. As a result, thirteen sample obligations had unliquidated balances as of September 30, 1996 which exceeded forward funding guidance by $1,655,504. However, because these funds were programmed to be spent prior to September 30, 1998, none of the thirteen obligations was considered excessive as of the time of audit. Following is a discussion of the principal amounts of excessive forward funding identified in our audit sample.

Of the $1,655,504 in obligations found to be excessive, $748,95 1 involved two obligations ($379,080 and $369,871, as shown in Appendix III) made in fiscal year 1995 for follow-on activities related to projects scheduled to end during fiscal year 1996. Rather than closing the predecessor projects and deobligating remaining funds, USAID/Honduras extended the completion dates of the projects after already obligating new funding for the follow-on activities. The extension of these projects delayed the use of the funds for the follow-on activities, resulting in large balances for the two obligations. These large balances were, in our opinion, inconsistent with USAID's forward funding guidelines and $748,95 1 was excessive as of September 30, 1996.

Another sample item, related to a grant to the Honduran Ministry of Health, also had an excessive unliquidated balance as of September 30, 1996 totalling $42 1,694. This amount was to fund costs to be 'incurred after September 30, 1997 and therefore exceeded the forward funding guidelines. In addition to the above, excessive forward funding totalling $484,859 was identified in ten other sample items during the audit. Details of these amounts are shown in Appendix III.

USAID/Honduras did not include consideration of USAID's forward funding guidance in its Section 13 11 review procedures, and Mission officials stated that they did not believe it was possible to properly manage ongoing projects in accordance with the existing guidance. The Mission considered 15 to 18 months of funding an appropriate level to manage its program and pointed out that funds often are not provided to the Mission until very late in the fiscal year, impairing its ability to finance program activities while complying with the guidance. They cited as an example that the Mission received $20.3 million of its 1997 funding in the fourth quarter of the fiscal year; however, annual work plans prepared by the Government of Honduras normally cover calendar years rather than fiscal years. Therefore, when funds are received late in the fiscal year, the Mission is unable to make obligations for the last quarter of annual work plans without violating the forward funding guidance. They emphasized the importance of fully funding USAID's commitments to host-government institutions and felt that compliance with USAID's forward funding guidance would be more feasible if funds were provided early in the fiscal year. A final point raised by the Mission was that the funding for some activities is Congressionally earmarked and the Mission has limited control over the amounts received, making adherence to forward funding guidance sometimes unrealistic in these circumstances.

While noting the above comments, we believe that the Mission would improve its adherence to USAID's forward funding guidance by including consideration of the guidance in its local operating procedures for conducting its Section 13 11 reviews. This would allow timely identification, analysis and, as appropriate, resolution of forward funding levels exceeding current guidance. The points raised by the Mission will also be considered, along with the views and experiences of other USAID offices, in preparing the Office of Inspector General’s summary report consolidating the results of the worldwide audit of USAID's review and certification of unliquidated obligations for project and non-project assistance.

> **<u>Recommendation No. 1</u>: We recommend that USAID/Honduras revise its local operating procedures to include consideration of USAID's forward funding guidance in its Section 1311 reviews.**

In addition to the above, the audit sample included two unliquidated commitments that were excessive as of September 30, 1996. These amounts, totalling $30,602, were no longer needed and should have been decommitted at year end. One was not decommitted due to an oversight by the Mission but was subsequently identified and decommitted prior to our audit. The other, related to severance costs on a personal services contract, had not been decommitted because the accountant performing the Section 13 11 review was not aware that a subsequent contract also funded these costs. At the time of our audit, excessive funding under this contract totalled $20,704, which the Mission should take action to decommit.

> **<u>Recommendation No. 2</u>: We recommend that USAID/Honduras decommit the $20,704 excessive commitment, as shown in Appendix III of this report.**

Observations on Internal Controls

While conducting our fieldwork at USAID/Honduras, we observed that certain Mission procedures related to the review and certification of obligations for project and non-project assistance could be improved, as discussed below.

USAID Financial Management Bulletin, Part II, No. 14A, states that the accounting reports used in Section 13 **11** reviews must be annotated to show (i) the date of the review and the names of the reviewers, (ii) the decision made with regard to the individual obligation and commitment accounts, including the summarized rationale for the decision, and (iii) related actions that should be taken to appropriately adjust the affected accounts. Mission controllers must assure a high standard of documentation and level of analysis that would lead any auditor to conclude that (i) a careful review of each unliquidated obligation and commitment document was conducted, (ii) the review was properly documented, and (iii) the findings and conclusions are supported by the analyses and documentation.

The Mission's working papers documenting its Section 13 **11** review did not meet the above standards. The Mission conducted monthly Section 13 **11** reviews and, to document these reviews, the Controller's Office kept unmarked copies of the accounting reports reviewed and journal vouchers supporting actions taken on obligations and commitments determined to need adjustment. However, the Mission did not maintain documentation pertaining to the analysis of obligations and commitments which were determined to be valid and still needed. For example, two of five accountants had thrown away their annotated working copies of accounting reports and had no documentation of the analyses and decisions made on those obligations and commitments found to be valid and still needed. Consequently, we could not readily conclude that a careful review of each unliquidated obligation and commitment was conducted.

USAID/Honduras' current operating procedures are general in nature and do not establish documentation standards to be followed in performing Section 13 11 reviews. Since the Mission's review process is decentralized, with each project accountant responsible for his or her own analysis and documentation, we believe that the Mission would benefit by establishing documentation standards in its local operating procedures. These should include guidelines for uniform notations of decisions reached on each obligation and commitment, and specific instructions regarding the retention of supporting documentation.

> **Recommendation No. 3: We recommend that USAID/Honduras revise its local operating guidance to establish uniform procedures and specific documentation requirements for its Section 1311 reviews.**

Management Comments and Our Evaluation

USAID/Honduras generally agreed with the conclusions of our audit report and has taken action on the report's recommendations. With respect to Recommendation Nos. 1 and 3, USAID/Honduras has taken final action by revising its operating procedures to incorporate consideration of USAID's forward funding guidance and key elements of USAID's Financial Management Bulletin No. 14A. For Recommendation No. 2, USAID/Honduras has taken final action by decommitting $20,704 cited in the recommendation.

Scope and Methodology

This audit is part of the Office of the Inspector General's (OIG) worldwide review of the USAID's obligations for project and non-project assistance. The worldwide audit is limited to obligations for project and non-project assistance which had unliquidated balances on September 30, 1996. It does not cover obligations funded with U.S.-owned local currency, obligations for disaster relief, or obligations maintained by USAID for the Trade and Development Agency.

The Regional Inspector General/San Salvador audited USAID/Honduras' review and certification of unliquidated obligations for project and non-project assistance, as of September 30, 1996. The audit was conducted at USAID/Honduras, from June 22, 1997 through July 24, 1997, and was performed in accordance with generally accepted government auditing standards. In answering our audit objective, we performed limited testing of the reliability of the Mission's computer-generated accounting data; however our testing was not designed to determine the overall reliability of this data.

At the request of IG/A/PA, USAID/Honduras compiled a list of its obligations for project and non-project assistance which had unliquidated balances on September 30, 1996. The unliquidated balances on this list totalled $43,924,659. We randomly selected 30 obligations totalling $14,5 10,589 from the list for detailed audit testing. Random sampling will allow the OIG to make USAID-wide projections based on field work performed at a limited number of sites. Because the audit sample was designed as part of the worldwide audit, a materiality threshold was not established for our work at USAID/Honduras and our testing was not designed to provide reasonable assurance at the Mission level.

While conducting our fieldwork at USAID/Honduras, we also performed limited tests of compliance with USAID and Mission procedures related to Section 13 11 reviews and pipeline reviews of obligations for project and non-project assistance. Section 13 11 review refers to the review of obligations to determine if the requirements of 3 1 U.S.C., Section 1501 (a) (originally enacted as Section 13 11 of the Supplemental Appropriation Act of 1955), are met for the validity of the obligations.

Because the accuracy and completeness of the Mission's list was crucial to our ability to make USAID-wide projections, we interviewed appropriate Mission staff about their methodology in preparing the list and reconciled the list and its totals to other Mission reports.

Each obligation was reviewed to determine whether it was valid in accordance with the provisions of 31 U.S.C. 1501(a) and decisions of the U.S. General Accounting Office. The results of our field work at USAID/Honduras will be consolidated with the results of field work conducted at USAID/Washington and other missions and used to make USAID-wide projections.

We also reviewed the unliquidated balance of each selected obligation to determine whether, on September 30, 1996, the balance was needed, in full or in part, to cover anticipated expenses for reasonable future periods. In making these decisions, we considered USAID and Mission guidance for forward funding, activity-specific budgets and spending plans, actual disbursements, progress reports, and accruals. When amounts were questioned, we interviewed relevant activity managers and contracting or grant officers. We also considered prior audits and obtained written representations from Mission management on key assertions related to our audit objective. The results of field work at USAID/Honduras will be consolidated with the results of field work conducted at USAID/Washington and other missions and used to make USAID-wide projections.

In addition to capturing information and making calculations as of September 30, 1996, for USAID-wide projections, we determined whether the unliquidated balances of any obligation reviewed during the audit still had excess balances at the time of our field work. If so, we recommended that the excess funds be deobligated or decommitted as appropriate.

USAID/HONDURAS
MEMORANDUM

USAID

DATE : March 20, 1998

TO : Wayne J. Watson, RIG/A/SS

FROM : Elena Brineman, Mission Director EB

SUBJECT : Open Recommendations Under Audit Report No. L-522-98-00X-F

The Mission has reviewed the USAID/Honduras portion of the subject audit report and agrees with its findings and content. Corrective actions have been taken to implement the recommendations. Following is the Mission response:

Recommendation No. 1:

We recommend that USAID/Honduras revise its local operating procedures to include consideration of USAID's forward funding guidance in its section 1311 reviews.

Recommendation No. 3:

We recommend that USAID/Honduras revise its local operating guidance to establish uniform procedures and documentation requirements for its section 1311 reviews.

Mission response:

The Mission has drafted and is now circulating for clearances and signature a Mission Order for the purpose of outlining and expanding the essential elements included in part II of USAID Financial Management Bulletin Number 14 A. This Mission Order addresses Section 1311 Reviews and emphasizes the importance of, and requirements for, preparation and retention of complete sets of workpapers evidencing appropriate performance of a valid Section 1311 Review. Attached, please find a copy of the draft Mission Order.

Based on the above reported corrective action, we request that recommendation numbers 1 and 3 be resoved.

Recommendation Number 2:

We recommend that USAID/Honduras decommit the $20,809 excessive commitment, as shown in appendix III of this report.

Mission response:

The Mission has decommited $20,704 which is the difference between the amount identified in the audit report as an excessive commitment under Project No 522-0325, and the amount disbursed as eligible project expenses. Please see the attached Journal vouchers and the MACS PO4 commitment liquidation record.

Based on the above reported corrective action, we request that recommendation number 2 be closed.

APPENDIX III

Excessive Obligations as of September 30, 1996
As Determined by Audit

Obligation No.	Excessive Amount	Reason Considered Excessive
PA-522-93-0008	$10,996	Excessive Forward Funding
PA-522-95-0009	$63,818	Excessive Forward Funding
PA-522-94-0008	$19,631	Excessive Forward Funding
PA-522-96-00 11	$421,694	Excessive Forward Funding
CA-522-0389-A-00-54 11	$379,080	Excessive Forward Funding
PA-522-94-0004	$59,557	Excessive Forward Funding
PA-522-93-0005	$37,901	Excessive Forward Funding
PA-522-93-0004	$22,675	Excessive Forward Funding
PA-522-92-0004	$42,999	Excessive Forward Funding
PA-522-95-0007	$369,871	Excessive Forward Funding
PA-522-93-0010	$116,834	Excessive Forward Funding
PA-522-92-0008	$1,816	Excessive Forward Funding
PA-522-96-0002	$108,632	Excessive Forward Funding
Total	$1,655,504	

Excessive Commitments as of September 30, 1996
As Determined by Audit

Obligation &Commitment Number	Excessive Amount	Reason Considered Excessive
PA-522-92-0013/CO-522-0325-S-00-1131	$22,062	Funds No Longer Needed
PA-522-90-0020/PIO/P-522-0325-l-00108	$8,540	Funds No Longer Needed
Total	$30,602	

Amount Recommended for Decommitment
As of the Time of the Audit (July 24, 1997)
As Determined by Audit

Obligation & Commitment Number	Amount Recommended for Decommitment	Reason for IG Recommendation
PA-522-92-0013/CO-522-0325-S-00-l 131	$20,704	Funds No Longer Needed
Total	$20,704	